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19 April 1985

MEMORANDUM FOR: All Summit Analysts

FROM :

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SUBJECT : Summit Paper Distribution

1. Attached was hand carried to State, NSC, and Treasury on 17 April. The paper contains country-by-country (including EC) positions on:

- Economic Policy (Structural Adjustment and Exchange Rate Issues, pp. 1-15)
- Trade (pp. 16-23)
- International Monetary Reform (pp. 24-30)
- Relations With Developing Countries (pp. 31-37)
- Environment (pp. 38-44)
- Space Station (pp. 45-51)
- Strategic Defense Initiative (pp. 52-59)

As has become standard practice, the package will be used as the backbone for the State/NSC/Treasury briefing of the President just prior to the Summit.

2. My thanks to the diverse lot of you for your outstanding contributions.

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Attachment: as stated

State Dept. review completed

EURM 85-10073

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Bonn Summit:
Country Positions
and
Statements

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17 April 1985

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ECONOMIC POLICY

STRUCTURAL ADJUSTMENT

JAPAN

Comment: Japanese officials have made few public statements regarding the need for concerted action on the structural adjustment problem, viewing it largely as a West European problem. Bureaucrats in Tokyo are concerned, however, that Bonn participants will press Japan to help solve West European structural problems by stimulating Japanese demand for imports. To blunt such attacks, Prime Minister Nakasone will point to efforts already under way to open the Japanese market, while arguing that Japan's severe budget situation prohibits adopting stimulative policies.

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WEST GERMANY

West German officials see eye-to-eye with the United States on the need to tackle structural economic rigidities. Bonn's annual economic report for 1985 states: "All experience shows that restructuring occurs faster and more efficiently in a free market rather than through bureaucratic direction.... The federal government therefore will actively continue its market-oriented restructuring policy. Key elements of this policy are more flexibility and mobility of labor and capital...."

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Comment: Structural adjustment is a major summit theme for Chancellor Kohl because he believes West European economies must become more flexible if the present high levels of unemployment are to be brought down. As a result, he will support US calls for new efforts to promote structural adjustment and technological change in the summit countries. Bonn has already taken some action in this direction and further efforts are in progress. A major easing of West German labor market rigidity should occur within the next few weeks because the Bundestag is expected to pass legislation reducing limitations on the use of part-time workers, widening employer discretion in setting work hours, introducing new flexibility in hiring and firing, and lifting curbs on the employment of women and young people. The Bundesbank also is planning to loosen capital market restrictions over the next few months.

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FRANCE

President Francois Mitterrand has made modernizing the French economy with "social justice" a favorite theme over the past year. Last fall in the economically depressed region of Lorraine, he told demonstrating workers that the government would help firms facing temporary difficulties but would not try to save companies that had not made an effort to remain competitive in international markets. French leaders have insisted repeatedly that even nationalized firms must make profits or face a change of management. This message was driven home when Bernard Hanon, President of Renault, was forced to resign because of the poor financial condition of the company.

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Prime Minister Fabius argued in a press conference last September that France's future depends on rapid adjustment to "sweeping, global changes." This modernization would require retraining the workforce, and he outlined a "colossal effort to harness the nation's only natural resource -- its human potential."

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Comment: The Socialists have made impressive progress, at least on paper, toward freeing the economy. They have taken preliminary steps toward reducing credit controls and have tried to create a venture capital market as well as an "over the counter" stock market. Paris has streamlined the process of creating a new business and has made it easier for employees or heirs to continue an old one. The Socialists even seem to have been able to eliminate de facto wage indexation, an accomplishment that the most optimistic supporter would not have expected three years ago.

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Foreign investors are now generally well received and can obtain authorization to invest fairly rapidly. In the past year, foreign firms -- especially Japanese firms -- have been allowed to buy troubled businesses that would have been bailed out in previous years. French firms have been actively encouraged to invest abroad and to form joint ventures, to create a permanent French commercial representation abroad rather than rely on hit-and-run sales.

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Although Paris will generally support the US position on the need for structural adjustment, some conflict on this topic could still arise. The French may try to discuss US budget deficits and high interest rates in the context of structural adjustment

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UNITED KINGDOM

In his March budget speech, Chancellor of the Exchequer Lawson summed up the Thatcher government's philosophy on structural adjustment.

The government's economic strategy has two key components: a monetary policy designed to bring down inflation and a supply side policy designed to improve the competitive performance of the economy. The supply side policy is rooted in a profound conviction, born of practical experience both at home and overseas, that the way to improve economic performance and create more jobs is to encourage enterprise, efficiency and flexibility; to promote competition, deregulation and free markets; to press ahead with privatization and to improve incentives....The argument over which will have a bigger impact on demand -- increased public expenditure or lower taxation -- completely misses the point. The case for lower taxation rests on supply side policy: lower taxes will help to enhance incentives, eliminate distortions, improve the use of resources and heighten the spirit of enterprise....The great mistake of postwar demand management, which still has some devotees today, was to react to rising unemployment by injecting more money into the system, whether through the budget or through the banks. Far from halting the upward trend of unemployment, this simply has generated runaway inflation.

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Comment: Prime Minister Thatcher is counting on tight fiscal and monetary policies and emphasis on free market principles to promote industrial restructuring and a sustainable economic recovery. Low inflation -- through slow wage growth, low interest rates, and a reduced budget deficit -- is key to her strategy. Selective tax cuts to spur investment and employment represent the other side of London's approach. The new budget, for example, introduced tax reforms to reduce the cost of hiring additional low income employees and promised additional support for youth training programs but only if the private sector carries the major cost burden. The budget, however, contains no new initiatives to attack the immediate problem of rising unemployment -- now over 13 percent of the workforce.

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Thatcher is determined to limit the role of government in the economy. The Tories advocate minimal public involvement in industrial affairs and are continuing their extensive program to return state-owned assets and corporations to the private sector. As a counterpart to this program, the government has deregulated several service sectors and introduced competitive bidding to the provision of some services previously provided exclusively by public workers. Key to the success of these two programs is reducing excess productive capacity and overmanning, while redirecting investment to the most efficient activities of the nationalized industries and services.

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The Prime Minister also appears prepared to take a tough line with the unions because she is convinced that reducing union power is an essential ingredient to long-term economic growth. She sees her victory over the miners as a step in that direction. Moreover, Thatcher has promoted legislation intended to curb union power. Last summer, Parliament passed regulations requiring the regular election of union officials -- a sharp change from the past when many union officials effectively headed their unions "for life". [REDACTED]

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ITALY

Italian policymakers have frequently expressed the need for industrial restructuring and Prime Minister Craxi recently stated that Italy "is preparing to confront the new industrial revolution." Craxi added, however, that the inflexibility of the Italian labor force could act as an obstacle to solving the problem of unemployment and revamping the economic system.

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Comment: Rome is well aware of the need for structural adjustments in order to keep Italy competitive. The government is funding programs that provide below-market financing for investment in machinery with a high technological content -- especially numerically controlled machine tools. Rome also is providing more research and development funding and restructuring the national research center to improve coordination between private and public research projects. In addition, Rome is now debating measures to cut labor costs, focusing in particular on easing rigid hiring and firing policies

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Italian firms in both the private and public sectors are vigorously pursuing their restructuring efforts. Last year alone, the industrial labor force dropped by over 300,000 workers as firms trimmed their workforce to cut labor costs. Italian companies in both the public and private sector are aggressively seeking joint ventures with foreign firms -- especially US firms -- to acquire technology, cut down on research and development costs, and obtain much-needed capital infusions. Italian firms are also trying to trim inventory holdings, automate production, and either diversify their product offerings or move into higher value-added products.

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Italy's restructuring efforts, however, continue to be limited by a number of factors, many of which will probably take considerable time to change. Investment spending on new capital equipment is still limited by high real interest rates, reflecting a growing budget deficit that the Treasury estimates will reach over 17 percent of GDP this year. Firms in the state sector, despite making important reductions in the workforce, are still burdened with maintaining redundant labor for socio-political purposes. Italy's capital markets remain underdeveloped, leaving Italian firms undercapitalized. Despite the provision of government funds for capital investment, firms often do not use allocations to full advantage because of bureaucratic inefficiency. Moreover, Italy's firms are still faced with a burdensome wage indexation system, the scale mobile, which will only be moderated after extended negotiations among government, labor, and business.

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CANADA

The major theme of Finance Minister Wilson's Economic Statement last November was the need to reduce the budget deficit in order to create an environment conducive to private sector growth and economic adjustment. Wilson indicated that the government has adopted a more positive stance toward foreign investment and that this will "attract the capital necessary to create new job opportunities, attract new technology and introduce new production processes and management systems, all of which will make our industries more competitive." A statement by several provincial premiers also recognized that "economic adjustments will have to be made if investor confidence is to be rebuilt and Canada's competitiveness restored."

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Comment: Although Mulroney believes that structural adjustment is critical to sustained economic growth, reduced unemployment, and low inflation, his government has moved slowly in this area. Mulroney's fears of controversy and obsession with consensus-building have thus far prevented any real progress. The Tories have introduced legislation to abolish the Foreign Investment Review Agency (FIRA) in order to reduce the barriers to foreign investment. The government has also implemented changes in the National Energy Program to encourage investment in this area.

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EUROPEAN COMMUNITY

Speaking to the European Parliament in January, Commission President Delors admitted that "European industrial society used to be a model of efficiency; it is less so today....It is fighting for its life....It depends on our strength and our ability to adapt our structures and stimulate an economic upturn at the same time." Delors pledged to work to break down the remaining barriers to internal EC trade and create a large market based on industrial cooperation, while promoting the convergence of EC economies to lead to higher growth and more jobs.

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Comment: EC leaders are not convinced of the utility of collective efforts to promote restructuring. The Ten accept the need to reduce the barriers to internal EC trade but do not agree on how to approach deep-seated domestic economic rigidities such as high social welfare costs, high taxes, and strong labor unions. During the Summit, Delors probably will point to the limited progress the Community has made in restructuring particular industries -- such as steel and textiles -- as evidence of EC willingness to adopt some of the painful measures necessary for economic restructuring. The Commission will continue to push high technology, but the lack of sophisticated European venture capital markets, the poor entrepreneurial climate, and EC budget constraints will hamper the Commission's efforts.

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EXCHANGE RATE ISSUES

JAPAN

During a late January press conference, Foreign Minister Abe insisted the strong dollar was partly responsible for the bilateral trade imbalance. Finance officials made similar statements during a period of renewed yen weakness in early February. In contrast, Prime Minister Nakasone remained silent on exchange rate issues during his 2 January summit with President Reagan, a silence subsequently criticized by Japanese journalists [REDACTED]

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WEST GERMANY

Speaking in Frankfurt on 23 February, Finance Minister Stoltenberg said, "Even the strongest economy on earth cannot live in the long run with a dramatically growing trade and balance of payments deficit....An early reversal in the dollar exchange rate to a more realistic level and subsequently to better-balanced terms of trade" is in the mutual interest of the United States, other industrialized nations, and the highly indebted Third World. Disdainfully addressing the "starry-eyed admirers of the dollar's strength" and those who scorn West European economic performance," Stoltenberg referred to the 4-percentage point gap between US and West German long-term interest rates. "The goal must be to close this gap by reducing the US budget deficit," he said, "not by raising interest rates in West Germany."

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Bonn will acknowledge that the strong dollar and US trade deficit have provided an important stimulus to world trade -- West German exports to the United States rose 43 percent last year. Moreover, the recent easing of the dollar exchange rate should alleviate somewhat its potential as a problem issue. Nevertheless, Bonn views the surge of the dollar earlier this year to the highest level since mid-1971 as a major risk for the world economy, and is increasingly restive about what it perceives as US benign neglect of exchange rates and deficits. Specifically, Bonn will complain that the strong dollar and US trade deficits are constraining monetary policy abroad, intensifying protectionist pressure in the United States, generating an export bias in US trading partners that is not likely to be sustainable, and threatening to reignite West German inflation.

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FRANCE

Finance Minister Bereznevoy told the IMF in September that "all our efforts should center on the need to prolong the world economic recovery." More recently, he told the press that while the high dollar created "inconveniences," such as increased import costs, it also had the advantage of boosting competitiveness. He observed that "in order to confront the American challenge, Europe . . . must rechannel capital now being drawn to the United States by its rediscovered dynamism and . . . by the budget deficit." Bereznevoy worries publicly that slow growth in Europe, and particularly in France, will widen the technology gap with the US and Japan. Foreign Trade Minister Edith Cresson echoed this view in a recent press interview when she said that "foreign capital flows are financing the US budget deficit, inhibiting needed European investment."

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Comment: The French believe that the strong dollar, high interest rates, and volatile exchange rates are a threat to the world recovery -- and are a particularly serious problem for the LDCs. Paris wants interest rates to fall both to encourage investment and to reduce the debt burden of the LDCs. At the same time, however, the French are worried that once the dollar begins to fall it may drop rapidly, damaging their competitiveness. They are particularly concerned with the impact a declining dollar could have on their high-tech industries.

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UNITED KINGDOM

Prime Minister Thatcher is pleased with the recent strengthening of the pound and stated in Parliament that "the exchange markets of the world are taking a different view of the dollar and are also realizing that the underlying strength of the British economy is very good for investment." The falling pound at the beginning of the year placed Prime Minister Thatcher in a difficult political and economic position, especially after she stated flatly "that the pound should stay above parity with the dollar." She also has said "that the value of a nation's currency reflects a country's basic strength," a notion her opponents were quick to exploit [REDACTED]

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Chancellor of the Exchequer Lawson, in the March budget speech, reaffirmed the government's determination to contain inflation and restore confidence in the pound, stating that "we have already shown that we are not afraid to take action, however unpalatable, to keep the Medium Term Financial Strategy on course in an unpredictable and uncertain world." The Chancellor also pointed to the US as the cause of most of Britain's problems with sterling. He said "if at home the past year has been overshadowed by the coal strike, internationally it has been dominated by the relentless surge of the dollar, which rose by a further 30 percent against all the major currencies. To finance its massive budget deficit the United States is importing a large part of the rest of the world's savings and exporting some of its own inflation. This is not a sustainable state of affairs."

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Comment: Prime Minister Thatcher is worried that high British interest rates -- increased in January to defend sterling and prevent an increase in British inflation -- could worsen the unemployment problem. The Prime Minister is likely to join other leaders in criticizing the US budget deficit at the Summit, especially if the dollar regains strength on international markets. The Prime Minister is more likely to take further domestic actions to support sterling if the pound shows weakness against major European currencies, than if it should fall only against a strong dollar. Thatcher does not believe that exchange rate intervention can alter underlying market trends, but she may push for renewed agreement on coordinated intervention by central banks when necessary. [REDACTED]

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ITALY

In February, Treasury Minister Gorla told reporters that "the EC doesn't have any simple solutions for correcting the imbalance in the international financial system caused by the strong dollar....A policy of constantly complaining doesn't produce results....The situation we are faced with now is one we may be living with for some time in the future." Industry Minister Renato Altissimo looked at the bright side: "The lira's weakness against the dollar can have positive effects if our industrial system can quickly adapt to the possibilities offered by the situation for major penetration by our products."

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Comment: The lira's depreciation against the dollar has helped to sustain export growth; exports to the US jumped by over 50 percent in 1984. Although the strength of the dollar continues to attract considerable attention in Italy, Italian policymakers are more worried about the lira's relative strength within the EMS. Italy's inflation rate, the highest among the Big Seven last year, and the relative stability of the lira within the EMS have led to a decline in Italian competitiveness in major EC markets.

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With regard to exchange markets, the major policy debate in Italy is over why the lira has remained stable in the EMS. One group, supported by Prime Minister Craxi, argues that the lira's strength within the EMS comes from capital inflows attracted by high real interest rates. This group, which gives priority to expanding employment, believes that the monetary policy fostering these high real interest rates is counterproductive. The second group, led by the Treasury and the Bank of Italy, believes that the lira's strength has technical roots, owing much to the strength of the dollar. These officials believe that fighting inflation should be the government's top priority and that reflation should take a back seat. Both groups would welcome a realignment of the EMS. The former would like to accomplish this through a shift in domestic monetary policy; the latter group, whose opinion seems to be gaining ground, expects that it can only happen if the dollar slips against the West German mark, which in turn should cause the lira to weaken within the EMS.

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CANADA

The Mulroney government has expressed concern about the need to keep Canadian interest rates above US levels in order to protect the value of the Canadian dollar. Finance Minister Michael Wilson has attributed high interest rates to "the significant financing requirements associated with the large federal deficits in the US, combined with fairly restrictive US monetary policy." He has stated that "continued high interest rates and growing debt will undermine confidence, put upward pressure on interest rates and reduce prospects for economic growth." For real interest rates in Canada to fall, he continued, there must be "further US deficit reduction measures and a complementary adjustment in monetary policy."

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Mulroney has acknowledged that "Canada also has a serious debt problem that requires responsible fiscal action," but Bank of Canada Governor Bouey has said that "even if other countries curb their deficits, they will still be subject to the same pervasive effect of US interest rates. There can be no question that a significant reduction in the high international interest rates requires credible deficit reduction in the US." Wilson also believes that the idea of periodic international coordinated interventions to maintain stability in the foreign exchange market are "a good thing" and should be used when necessary.

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EUROPEAN COMMUNITY

Top EC Commission officials have on several occasions criticized the strong US dollar and the US budget deficit. During a February press interview, Willy De Clercq, the EC Commissioner in charge of external affairs, argued that the United States must act more forcefully through exchange rate intervention to restrict dollar fluctuations. De Clercq warned, "One must say, however, that the position of the United States is disappointing....An unchanged US policy can result in dangerous tensions between America and Europe." In late February comments leveled at US international monetary policy, Delors asked rhetorically, "How can a country behaving like this really say it is running the world's economy?" Echoing the theme of US international economic responsibility, West German Economics Minister Bangemann, speaking on behalf of the EC, said in mid-April that the United States "cannot, as the leading industrial and political power in the world, make policy without considering how these policies affect international trade and currencies."

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Comment: Delors is likely to argue in Bonn that there is a connection between Europe's unemployment problem and the global financial situation. Diplomatic reporting indicates he believes that the strong dollar -- which he links to the US budget deficit -- is draining capital out of Europe and inhibiting job creation. Delors almost certainly will argue for more effective coordination of exchange rate intervention. He probably will maintain that a hands-off attitude toward foreign exchange markets permits excessive currency fluctuations that strain trade relations. Delors may point to the virtues of the European Monetary System's fixed exchange rate regime, which he believes provides the international monetary system an important bloc of monetary stability.

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TRADEJAPAN

In keeping with his desire to see Japan play a more active role in international affairs, Prime Minister Nakasone has taken every opportunity to endorse a new GATT round that would focus on services, high technology, and agriculture. The Prime Minister, for example, raised the subject -- eliciting a positive response -- during the January visit of West German Economics Minister Bangemann. His government also announced a package of market-opening measures in early April to provide wider access to Japanese markets.

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Comment: Nakasone will support US efforts at Bonn to achieve a firm agreement to open the new round next spring. The Prime Minister's support for import liberalization, as evidenced by his personal interest in ongoing US-Japan trade talks, is designed partly to deflect growing criticism of closed Japanese markets. If pressed at Bonn, Nakasone is likely to point to recent "successes," such as last December's trade package and the liberalization of the financial market, and claim that Tokyo is moving as quickly as possible to open other markets.

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WEST GERMANY

The rejection of protectionism and defense of free trade runs throughout the international section of Bonn's annual economic report for 1985: "Protectionism does not help keep jobs but contributes to their loss....There is no alternative to free trade....The (West German) Council of Economic Advisors is fully justified in saying that the alpha and omega of all international tasks is opening the markets of Europe wider and reducing protectionism worldwide....Unfortunately, the work program agreed to at the November 1982 GATT Ministerial has met with quite modest results to date. The task of comprehensive, multilateral negotiations on liberalizing trade in a new GATT round has therefore become all the more necessary. The federal government will strive this year for intensive preparations for a new round ...in order that the round can begin in 1986."

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Comment: Chancellor Kohl wants to ensure that the Summit communique strongly emphasizes free trade; he supports an early 1986 date for the start of multilateral trade negotiations. A sense of urgency exists in Bonn that if agreement to begin a new trade round in 1986 is not achieved this year, protectionist pressure in the United States and EC will become unmanageable.

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Kohl almost certainly will condemn protectionism in general and closed Japanese markets in particular. He probably will avoid criticizing US protectionism as part of an overall West German strategy to associate himself with US economic success.

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FRANCE

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President Mitterrand told American businessmen in 1984 that France is "opposed to protectionism," and later warned French workers that France would not resort to protectionism to aid inefficient firms. Many French policymakers, however, are worried about increased protectionism in the United States.

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Comment: Despite public statements opposing protectionism, France is in no hurry to start new multilateral trade negotiations. Paris fears that a new trade round will call into question the EC's Common Agricultural Policy and agricultural export subsidies. Paris also is concerned that special rules for trade in services would favor the development of US services to the detriment of some emerging high value-added French services. French officials also will argue that a new round is not supported by the LDCs because they see nothing to gain. The French believe that the main impediment to trade now is unrealistic and volatile exchange rates -- the dollar problem.

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UNITED KINGDOM

Secretary of State for Trade and Industry Norman Tebbit told US Embassy officials in March that "the UK favors a new trade round and will work within the Community to develop a position compatible with US objectives." The British think that it is essential to involve LDCs from "Bangladesh to Brazil" in the talks. Representatives from the Foreign Office wonder if the industrialized countries would "be willing to give up the multi-fiber agreement" to draw in the LDCs, although admitting that "UK thinking on this is at a very preliminary stage."

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Comment: The British, who face domestic pressure for increased protectionism themselves, are anxious to discourage such trends. They depend on foreign commerce for close to 30 percent of GNP, and believe that maximum gain from their domestic recovery is unattainable without free trade. London probably will agree to a Summit declaration launching a new trade round in 1986, but will insist that the US clarify its objectives for the talks. Tebbit, a close Thatcher ally, recognizes that there are strong protectionist pressures in the US; while he applauds Washington's recent decision not to renew voluntary quotas on Japanese autos, he has expressed concern about US farm legislation that could harm the EC's CAP.

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ITALY

[REDACTED] Renato Ruggiero, Rome's Sherpa and newly appointed Secretary General of the Foreign Affairs Ministry, told US officials last year that his government agreed on the benefits and the appropriateness of eventually moving to a new round of trade negotiations, but believed that the industrial nations should complete their protectionism rollback first. More recently, in early April the Chief of the Foreign Ministry's OECD Affairs Section expressed skepticism over Japanese support for a new round, commenting that the Japanese might use it to stall on promised import promotion measures. In addition, he stated that there should be a stand-still understanding so that governments would not adopt new import restrictions and then bargain away the new measures. [REDACTED]

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CANADA

The Canadian government has expressed a desire to "obtain more secure and improved access to foreign markets on the broadest possible basis" in order to foster growth. "This would require, of course, that Canada would also have to increase access to its domestic market....The government will examine all avenues to secure and enhance market access...(including) preparations for and opportunities provided by multilateral trade negotiations." Nevertheless, Mulroney affirmed that he would defend Canada's interests, saying that in today's international protectionist environment Canada would have to "work in the world as it is and cannot afford to play Boy Scout."

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Comment: Canada relies heavily on exports -- about one-fourth of Canadian output is exported annually -- so it has much to gain from freer global trade. Ottawa strongly supports a new multilateral trade round and hopes it will help curb protectionist sentiment in the US Congress. Easy access to US markets is vital for Canadian exporters and they fear that US protectionist measures aimed at other countries might have a negative effect on Canada's exports as well. Mulroney believes, moreover, that the Summit leaders may have to make concessions to LDCs for their support of a new trade round.

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EUROPEAN COMMUNITY

The proposed new trade round will be the EC's major concern at the Summit. The Council conditionally endorsed the new round in mid-March, "subject to the establishment of an adequate prior international consensus on objectives, participation and timing." The Council declaration signaled EC willingness to discuss trade in services, but it failed to mention high technology and stated that the fundamentals of the EC Common Agricultural Policy "shall not be placed in question." It added that "results in the monetary and financial areas should be sought in parallel with results in the trade field," and asserted that "it is a pressing political necessity" that Japan increase imports. Although the declaration avoided committing the EC to a date for launching the new round, an earlier Commission paper recommended late 1986 or 1987.

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Apart from the new round, many recent EC trade statements have dealt with US policy on semi-finished steel and steel pipe and tube imports. The Council warned in late March of the danger of "a profound deterioration of the relations between the Community and the United States" over the steel issue.

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Comment: The timing and agenda of the new round are especially sensitive issues for the Community because of differences of opinion among EC members. Delors is likely to act cautiously to accommodate all members' views. He probably will try to avoid committing the Community to a specific date for launching the new round, arguing that the timing issue should be put off until the preparatory meeting set for this summer. He will almost certainly also hold out for a commitment on monetary discussions before agreeing to start the trade talks. Delors may try to use the steel issue to deflect US calls for a new round, arguing that US protectionism must be stemmed before new trade talks can begin.

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INTERNATIONAL MONETARY REFORM

JAPAN

Japanese officials have made few recent public statements regarding the issue of international monetary reform. [REDACTED]

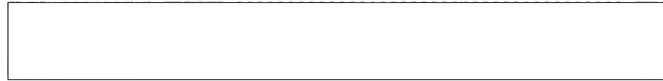
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[REDACTED] Comment: Tokyo does not want to link the initiation of a new trade round with the issue of international monetary reform. Moreover, Japanese officials doubt that the French idea of exchange rate target zones is practical; they argue that the economic performance and policies of industrial countries are too divergent to enable such a system to operate. [REDACTED]

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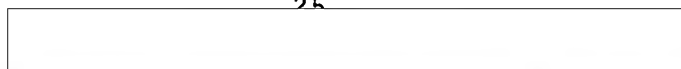
WEST GERMANY

Economics Minister Bangemann, in a meeting with Deputy Secretary Dam on 4 April, said that West Germany does not favor major reform of the international monetary system. He contended, however, that monetary and trade issues are linked and should move in parallel but separate forums. He said the Summit must find a multilateral compromise solution to this problem.

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FRANCE

Finance Minister Bereznevoy told the annual meetings of the IMF last fall that "monetary stability is a necessary condition for lasting growth....The weight of the LDC debt, aggravated by the rise of the dollar is a threat to world recovery....We all sense that the international monetary system must be adapted to the great social changes taking place." He concluded, "The Group of Ten had developed useful ideas...on the stabilization of exchange rates, international liquidity, multilateral surveillance, and the role of the IMF....France hopes a special meeting of the Interim Committee will debate these issues in 1985."

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Comment: The French obtained a commitment at the Williamsburg Summit to study the international monetary system; they think it is now time to move toward reform and hold that discussions be held in tandem with any multilateral trade negotiations. Paris has two basic objections to the current international monetary system: exchange rates are too volatile, and the US has the advantage of printing the de facto world money because dollars are the primary reserve asset for both official and private holdings. The French have suggested that they would like to see a system of target zones for exchange rates between the dollar, the ECU, and the yen, but they have not outlined a system for maintaining the zones, other than through greater intervention. They would like to see the ECU and probably the yen used more in international transactions and in reserve holdings but again have not suggested reforms to achieve this goal. While Paris favors more short-term central bank coordinated intervention, it has not really advocated long-term policy harmonization. The French also generally argue for a new issue of SDRs and a better financial deal for the LDCs as part of their monetary reform proposals.

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President Mitterrand probably will welcome the recent US proposal for an international monetary conference, but he may insist that the US initiative does not go far enough. At the Summit the French may treat the conference as a fait accompli and ask their Summit partners to approve a conference agenda that includes specific issues of interest to France.

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UNITED KINGDOM

[REDACTED] Undersecretary for Trade and Industry Roy Williams told US Embassy officials in March that the British "will seek to ensure that . . . any action on the monetary side be taken in parallel with the trade round but not conditional upon it." [REDACTED]

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Comment: London almost certainly is interested in discussing international monetary problems at the Summit, but the British do not support French proposals that imply sacrificing control over domestic monetary policies to a system of target zones involving the yen and the ECU. [REDACTED]

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[REDACTED] 25X1

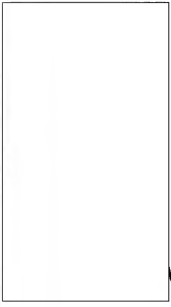
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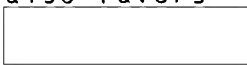
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ITALY

In a November speech at Harvard University, Lamberto Dini, Director General of the Bank of Italy and Chairman of the G-10, pinpointed current exchange rate uncertainty, interest rate volatility, and swings in international liquidity as key international monetary problems. Dini stated that the solution to these problems lies in closer coordination of economic policies and cited the G-10 studies on multilateral surveillance as a starting point. He also suggested that clear rules for conducting multilateral reviews should be established. 

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Comment: Craxi is not likely to raise the issue of international monetary reform at the Summit, nor will he demand a linkage between monetary reform and a new trade round. The Italians believe that a flexible exchange rate regime is the only viable system in a turbulent economic environment and that exchange rate stability can be achieved only if major countries harmonize domestic economic policies. Moreover, Rome wants the IMF to play a more active role in multilateral surveillance and to include all G-10 countries. The Italians believe that the multilateral surveillance process can be improved by having semiannual meetings, basing discussions on analytical papers prepared by the IMF, meeting prior to policy formulation in major countries, and going public with the results. Italy also favors expanded use of the ECU and a new allocation of SDRs. 

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CANADA

At the Commonwealth Finance Ministers Conference in September, Michael Wilson stated that "the world's financial system has been able to handle the debt crisis of recent years and (there is) no reason to change it radically." [REDACTED]

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Comment: Mulroney does not support Mitterrand's call for an international monetary conference to be linked with new trade negotiations. The Canadians, however, would be willing to discuss exchange rate problems because Canada is greatly affected by fluctuations in the foreign currency market. Mulroney shares French concerns over the volatility of exchange rates but almost certainly would not agree to a system of target zones involving the yen and the ECU. The Prime Minister supports the French position that SDRs should be increased and a better financial deal should be given to LDCs. [REDACTED]

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25X1

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EUROPEAN COMMUNITY

In a January press interview, Delors said, "I took the (EC) monetary affairs portfolio for myself, because I am tenacious....I will not stop making monetary proposals and I have a lot to say." Delors has made strengthening the European Monetary System one of his priorities, arguing that "a substantial strengthening of monetary cooperation and a controlled extension of the roles of the official and the private European Currency Unit (ECU) are both possible." During talks with a former US official in January, Delors argued that the world should move toward a three-currency reserve system, in which the yen and the ECU would become more acceptable substitutes for the dollar. Delors has also championed linking the proposed new GATT round to monetary reform. According to diplomatic reporting, Delors was instrumental in inserting language in the EC declaration on the new round calling for parallel trade talks.

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Comment: Delors, a former French finance minister, has been a long-time advocate of international monetary reform. His recent statements indicate, however, that he approaches the issue pragmatically and recognizes that a return to fixed exchange rates or a complete overhaul of the international monetary system is not possible in the near future. At Bonn, he probably will welcome the US proposal for a high level meeting on monetary issues. Together with French President Mitterrand, Delors is likely to try at the Summit to pin the United States down on the monetary talks, reminding US officials that the Community still considers this the quid pro quo for cooperation in the new GATT multilateral trade round.

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RELATIONS WITH DEVELOPING COUNTRIESJAPAN

In late 1984 Prime Minister Nakasone stated that Japan must spare no effort to help the developing nations; economic assistance is expected to increase about 10 percent this year. Budget austerity, however, will prevent the Japanese from reaching their goal of doubling aid between 1981 and 1985. Tokyo has also proposed a capital increase for the World Bank, subject to increased conditionality of lending and administrative reform of the Bank. Japanese officials repeatedly have stated the LDC debt problem should be handled on a case-by-case basis and creditor nations should maintain open markets and low interest rates.

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25X1

Comment: Japan has spoken out on behalf of the LDCs primarily because it relies on them for raw materials and export markets. Tokyo also views aid as a way to demonstrate it is a responsible ally who supports Western interests. Tokyo has increased aid to Africa and called for closer cooperation with industrial nations in seeking solutions to the region's economic and political problems.

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WEST GERMANY

In a March newspaper interview, Chancellor Kohl said that "the North-South conflict would surpass the East-West conflict in importance by the end of this century or beginning of the next." Accordingly, Bonn stresses strengthened cooperation with the developing countries and their further integration into the international economic system. The West Germans believe this can best be achieved through steady expansion of trade and opening developed country markets to LDC products. On Third World debt, Bonn sees no alternative to the current, case-by-case approach. In a February speech Finance Minister Stoltenberg also stressed that "lower dollar interest rates are an essential precondition for keeping the international debt crisis under control and eventually solving it."

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Comment: Bonn wants the Summit countries to reaffirm their will to maintain or increase aid, as well as their continuing support for the international financial institutions -- but without making any major new aid commitments. On Africa, Bonn wants a Summit commitment to continued emergency food aid that also underscores the importance of overall development aid and greater African food self-sufficiency.

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Bonn hopes the Summit participants will state their willingness to negotiate more multiyear debt reschedulings where appropriate and express their approval of the loan restructuring efforts being made by commercial banks on behalf of countries making adjustment progress.

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FRANCE

Last September, Finance Minister Beregovoy told the IMF/World Bank meetings that "a reduction in interest rates would be welcome, but would not be enough to counter the weak expansion of international liquidity that threatens growth....We are in favor of a new allocation of SDRs. France also supports enlarged access to the IMF." Beregovoy was critical of the results of the 7th replenishment of IDA funds as well as recent trends in World Bank aid. He expressed France's support for a general increase in World Bank capital and also called for a "special facility for Africa."

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Comment: Traditionally a large aid provider, France will support almost any initiative to increase aid flows -- particularly to Africa, where Paris maintains close ties with many former French colonies. France seems reconciled for now to the case-by-case approach to debtor countries but would like to establish a precedent for multiyear rescheduling.

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[REDACTED] 25X1

UNITED KINGDOM

[REDACTED] London prefers to approach debt rescheduling on a case-by-case basis rather than by initiating global reforms. In addition, the British have become more selective in their aid disbursements as they reduce total government spending while trying to maximize British economic and political influence in high priority areas. [REDACTED]

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[REDACTED] Comment: The British have not changed their position on LDC debt issues since the London Summit, and the scarcity of comments on the topic by important officials may be an indication of a relative lack of interest. Thatcher probably would favor more coordination among the developed countries on North-South matters but, because of her continuing problems with the budget deficit, likely will oppose any major new aid initiative. [REDACTED]

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[REDACTED] 25X1

[REDACTED] 25X1

[REDACTED] 25X1

[REDACTED] ITALY

Rome believes the US case-by-case approach to the problem of LDC debt fails to acknowledge that certain solutions, such as lowering interest rates, are beyond the control of the LDCs and that significant international cooperation also is a requirement. In Rome's view, the US policy makes the LDCs' economic recovery primarily a domestic matter since it permits foreign investment only in the latter phase of the adjustment process. [REDACTED]

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[REDACTED]

Rome probably will continue its support for a capital increase for the World Bank, a move which some officials believe could appease the LDCs and head off calls for a special debt relief program. [REDACTED]

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[REDACTED]

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CANADA

[REDACTED] The Canadian government recently indicated that it believes a more explicit link should be made between the short-term adjustment of LDC debt and the issues of longer term growth and development, and recommended that the activities of the World Bank and the IMF be more closely coordinated in dealing with the LDCs. In addition, in late 1984 Ottawa recommended additional \$5 billion SDR allocations in 1985 and 1986 as a noninflationary means of assisting the LDCs. [REDACTED]

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Comment: Some or all of these proposals may be raised at the Summit. Ottawa traditionally has been a strong supporter of the North-South dialogue and this probably will continue. Under Mulroney, however, Ottawa's support will be much less flamboyant than under former Prime Minister Trudeau and will concentrate more closely on the purely financial aspects of the dialogue. [REDACTED]

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[REDACTED]

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EUROPEAN COMMUNITY

The EC and 65 African, Caribbean, and Pacific LDCs -- the so-called ACP states -- signed the third Lome Convention last December. Lome III will run for five years and provide the ACP countries more than \$5.8 billion in EC grants and loans. An ACP representative claimed, however, that Lome III "falls far short of the minimum requested by the ACP and justified by our needs." Despite this ACP grumbling, Commission officials describe the Lome Convention as "a political pact that helps to define Europe and hold the world in balance. The Community can have no political, economic, or strategic future in a world polarized round the superpowers unless it can forge a special positive relationship with the Third World." EC Commission President Delors recently attacked US policy on Third World debt, asserting that Washington is "just dropping loose change in the collection plate" in discussions of the debt issue.

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Comment: The financially strapped EC countries were in no position to significantly increase aid to the ACP countries and insisted on attaching more stringent conditions on how EC funds are used in the Third World. Despite its shortcomings, the EC still sees the Lome Convention as a model of North-South cooperation and is likely to point to its provisions in discussing development strategies. Delors believes that the EC can be proud of its record on North-South issues, and he may argue that the industrialized countries should make a more concerted effort to help the heavily burdened LDC debtors.

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ENVIRONMENT

JAPAN

Tokyo encourages international cooperation on the environment and believes environmental policies should consider industry, energy, and other scientific and socioeconomic aspects. [REDACTED]

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Comment: Although environmental cooperation is not a key issue for the Japanese, they will probably go along with what the Summit adopts without making waves. Tokyo considers acid rain a European and American problem, but believes it has shown concern for the environment by deciding against dumping radioactive waste in the Pacific. [REDACTED]

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WEST GERMANY

Rapidly worsening damage to West German forests from acid rain has pushed Bonn into the unusual position of taking the lead in Western Europe on an international issue. International cooperation on acid rain is a key priority for Bonn because 50 percent of the acidic materials falling in West Germany comes from foreign sources. Kohl calls the problem one of "inestimable importance" and points out that the German "love of the forests is an essential part of our national identity."

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Comment: Kohl will insist on some kind of Summit commitment to increased international cooperation in the environmental area. He has a personal interest in environmental protection and enjoys near-unanimous domestic support on the need for action. In addition, Bonn would like the Summit communique to state that economic growth and environmental policies are fully compatible, and that environmental policies should make maximum use of market-conforming incentives.

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Bonn views the United States as the leader on domestic environmental policy, but Kohl may urge the United States to be more forthcoming internationally. Although Bonn is conducting a major test of the effectiveness of speed limits in reducing acid rain, Interior Minister Zimmermann, whose ministry is taking the lead on handling the environmental issue at the Summit, terms the US 55 mph speed limit "ridiculous." The result, he said in an 8 March newspaper interview, is that US "highways are in a catastrophic condition, and the American automobile industry, technologically, is today in last place in the world."

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FRANCE

Comment: The environment is not a critical issue for the French, although the beginnings of a "green" movement are present. Paris has not been enthusiastic about West German initiatives and opposes adoption of American auto emission standards. The French are concerned that applying such standards would be expensive for their auto industry which is already having difficulties. Moreover, they argue that countries which have been exporting heavily to the US -- and have already adopted the technology -- would be at a competitive advantage.

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UNITED KINGDOM

The United Kingdom has refused to join the European "30-percent club" whose goal is to cut atmospheric pollution by 30 percent within eight years. Commenting on this refusal, Prime Minister Thatcher said that "the UK has cut emissions of sulphur dioxide by 40 percent since 1970 and by more than 20 percent since 1890." She concludes that the 30-percent goal "would be prohibitively expensive."

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Comment: London may feel somewhat defensive on the acid rain issue, but Thatcher will not accept actions that would dampen economic growth. At the Summit, the British probably will want to discuss environmental issues only in the broad context of economic growth and development, and will work to avoid commitments to reduce specific pollutants. The British support the US position that more research needs to be done to verify the link between industrial emissions and acid rain.

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ITALY

The Agriculture and Ecology Ministries are conducting a campaign to draw attention to the acid rain problem, and Italy is prepared to sign the Geneva convention on transboundary atmospheric pollution -- pledging to reduce sulfur dioxide emissions by 30 percent from the 1980 level. Italy will also support the EC proposal for uniform emission limits for large combustion plants.

Comment: Despite these positive steps, Rome is not yet ready to address the acid rain problem in either the domestic or international context, and favors more study before any major pollution abatement programs begin. The Italians, however, are particularly concerned about maritime pollution -- especially in light of the recent oil spill in the Straits of Messina -- and may seek to highlight the issue during Summit discussions.

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[REDACTED]

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CANADA

[REDACTED] Acid rain continues to be the overriding environmental issue in Canada and the Canadian media have criticized Prime Minister Mulroney for lack of action. [REDACTED]

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[REDACTED] Comment: Mulroney had been hoping that his recent meeting with President Reagan in Quebec City would result in substantive joint action aimed at reducing acid rain-causing emissions and almost certainly is disappointed that the resulting bilateral agreement called only for additional study. He probably will react to domestic criticism by arguing for a strong Summit statement on acid rain. This multilateral approach would be a reversal of policy, since earlier this year Mulroney indicated publicly that he wanted to confine the issue to Canada's bilateral agenda with Washington. In the wake of his meeting with the President, Mulroney probably will not take the lead on acid rain at the Summit, but he almost certainly will strongly support any initiatives from Chancellor Kohl. [REDACTED]

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EUROPEAN COMMUNITY

EC environment ministers agreed in early March to phase in Community-wide auto emission standards by 1994. Although the Commission said the measures "will achieve considerable reductions in atmospheric pollution," environmentalists dismissed them as "too little and too late."

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Comment: The agreement on emissions standards should help EC members avoid a confrontation with West Germany, which last year moved unilaterally to impose emission controls. The agreement leaves each EC country to choose the technologies for meeting the standards.

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SPACE STATIONJAPAN

Japanese government agencies and industry study groups are evaluating plans to provide experimental and logistical support modules that would attach to the space station. Tokyo has allotted nearly \$24 million for preliminary design of the project. The major thrust of the Japanese effort will be the commercial use of space, especially manufacturing pharmaceuticals and new materials.

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Comment: Tokyo's decision to participate in the project has touched off fierce competition between MITI and the Science and Technology Agency for the leading role in administering the program. Because of the emphasis on commercialization of space, MITI may have the edge in the interministerial fight. Continued bureaucratic bickering, however, could complicate existing budget-related problems and delay Japanese participation.

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[REDACTED] 25X1

WEST GERMANY

[REDACTED] The West Germans have endorsed participation in the US space station project, and Bonn feels the issue has been successfully resolved. [REDACTED]

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[REDACTED] 25X1




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FRANCE

25X1

President Mitterrand maintained before the Dutch Parliament in 1983 "that Europe should be capable of launching...an inhabited station" as a "great step toward its own defense." He argued to the European Parliament last May that having a space station project of its own would provide Europe with a yardstick for measuring US offers of cooperation. Other senior French officials, notably Prime Minister Fabius, have claimed that Europe needs its own space station as a mark of its greater responsibility for its own defense. 

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Comment: France has consistently deprecated participation in the US space station program. Mitterrand is therefore likely to resist any effort to produce a summit declaration favoring such cooperation. If pressed, however, he will probably acquiesce because he realizes that continued West German support for the French-led Ariane launcher program is in part contingent on French agreement to European Space Agency participation in the US space station project. Paris's long-term goal for itself and for Europe, according to US Embassy reports, is to achieve space autonomy (particularly for commercial applications) that minimizes -- and eventually eliminates -- dependence on US and Soviet systems. 

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UNITED KINGDOM

British Technology Minister Geoffrey Pattie said that "joining the space station program will give us access to all of the international space-station facilities for techniques such as satellite refurbishing and refueling. These will be essential if our space industry is to keep ahead of the competition into the next century." He also said that "Britain would urge the European Space Agency's other 10 members to respond positively to the invitation by the US that Western Europe should help in the construction of a manned space station, which is due to enter orbit in 1992."

25X1

Comment: The British view the space station not only as an opportunity for British industry but also as an opportunity to gain access to US technology, and they probably will seek assurances that participation will guarantee this. So far they have dedicated over \$8 million to set up a center -- the British National Space Centre -- to coordinate Britain's research efforts and to focus participation in a two-year feasibility study of the space station.

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ITALY

Italian space industry observers are predicting that 1986-90 will be the golden years for the industry in their country. Their optimism is based on the Italian industry's strong order books and on its flexible and realistic market strategy. In an overcrowded international market, Italy sees little advantage in competing in those products US space firms already produce but rather has attempted to develop a technological expertise that complements US developments.

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Comment: Italy is anxious to "participate in rather than contribute to" future US-Italian space efforts. Rome perceives the spacelab project as one in which Italy would wind up renting from NASA what it helped pay to develop. More specifically, any US steps to block a future offer by Europe to provide at least one of the modules for the space station could cause Italy to reconsider its efforts to strengthen cooperation with the US in space.

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CANADA

[REDACTED] Ottawa has recently announced that it will participate in the US space station program and that it anticipates spending about \$500 million over the life of the project. [REDACTED]

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[REDACTED] Comment: The Conservative government is committed to developing Canada's high technology industries and sees the space station as an avenue to promote growth in Canada's small but highly efficient aerospace industry. For domestic political purposes, Ottawa is anxious to publicize any information that portrays the space station as being unrelated to the development of military technology for use in outer space. [REDACTED]

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[REDACTED]

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EUROPEAN COMMUNITY

[REDACTED] The EC per se has not taken a position on the space station. All EC members except Luxembourg and Greece belong to the European Space Agency and coordinate their space station policy through that organization, not the EC. [REDACTED]

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STRATEGIC DEFENSE INITIATIVEJAPAN

Prime Minister Nakasone, during his 2 January summit meeting with President Reagan, expressed full support for the research phase of SDI. Subsequently, under pressure from the media and the opposition parties, he retreated to simple "understanding" of the US initiative and explicitly denied he had given full support to the overall SDI concept. In recent weeks, he has expressed willingness to extend technological cooperation with the United States. According to press reports, he also has tasked the bureaucracy to conduct independent studies of the technical feasibility and military implications of SDI.

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Comment: We believe Tokyo will continue to provide low-key, qualified endorsement for SDI research as long as it is premised on a firm linkage to the US-Soviet arms control talks and US willingness to consult fully with Japan. The Japanese Government recently reaffirmed this line in consultations with French and West German arms control officials. Thus far, the reaction in Japan has been muted, and one of the opposition parties has broken ranks and sided with the Prime Minister. With other issues moving to center stage and SDI difficult to understand, the government probably will continue to favor providing technological support for SDI research. It will, however, insist on extensive briefings and may not clarify its position in time for the Bonn Summit.

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WEST GERMANY

The West German position on SDI and participation in SDI research remains unsettled. Although Bonn still has made no final decisions, the Kohl government supports SDI research as a means to counter similar research by the Soviets and because it realizes there is nothing Bonn can do to stop it. Bonn also appears to be favorably disposed toward West German participation in this research, provided there is a "complete" exchange of technology. The government has hinted to the West German press that it is irritated by the 60-day deadline in Secretary Weinberger's recent letter on participation in SDI research. The Kohl government does not plan to arrive at any decision until it has consulted with its Allies and the Chancellor has had an opportunity to discuss the issue with President Reagan in May.

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The tone of West German statements, including those by the Chancellor, have become more critical in recent weeks. Kohl's speech at the Wehrkunde Conference in Munich in February was widely interpreted as an unconditional endorsement of SDI, contrasting sharply with the coolness toward the program expressed by the other Allies, particularly the French. Since then the Chancellor clearly has backed away from this position. On 20 March, he told the CDU national party congress that the Geneva talks could make the question of SDI deployments "superfluous" if the US and USSR agree on a major cutback in nuclear weapons. On the other hand, Kohl's chief foreign policy adviser, Horst Teltschik, who heads an intergovernmental working group on SDI, stated that the Geneva talks could result in a "mixture" of offensive and defensive systems.

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The Chancellor also told the CDU congress that his government will advocate a "joint European approach" -- to be urged on the US -- to the question of whether the systems actually will be deployed. Within a week, the Kohl government had modified this further to say that it would seek a joint European position even on the question of whether to participate in SDI research.

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Comment: SDI remains a difficult political issue for the Kohl government, and we believe Bonn would be reluctant to include an endorsement of the program in any formal Summit declaration. Above all, the West Germans remain concerned that large-scale deployment of ballistic missile defenses could result in a decoupling of Western Europe from the US nuclear deterrent. Key cabinet members -- Defense Minister Woerner and Foreign Minister Genscher in particular -- long have harbored doubts about the program. Chancellor Kohl personally has played a more important role on this issue than on many others, and we believe West Germany's relative support -- now apparently including Woerner -- thus far can be attributed to his personal desire to preserve good relations with the United States. At the same time, the Chancellor and his key ministers realize that they

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[redacted]

cannot stop the US research effort, that they stand no chance of influencing US SDI policy (particularly a decision to deploy) if they do not participate, and that Western Europe would drop further behind the United States in technology if Washington opted to proceed alone or in cooperation with Japan. We do not expect the opposition Social Democratic Party's total rejection of participation in SDI research to be a significant factor in the government's final decision. [redacted]

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The West Germans expect the United States to negotiate with the Soviets on SDI, and they no doubt foresee domestic problems if the Geneva talks on INF are seen to be stalled over the issue. The statements by Kohl and Teltschik indicate that Bonn sees a "linkage" between Geneva talks on nuclear and space weaponry. The "interrelationship" of the issues on the agenda in Geneva also is emphasized in an official announcement approved by the Federal Security Council on 27 March. All of these statements imply that the Kohl government has serious reservations about the direction SDI will take the Alliance.

[redacted]

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FRANCE

French policymakers have not reached a consensus on SDI, but many are clearly skeptical of its technical feasibility and concerned about the long-term threat defensive systems pose for the French nuclear deterrent. In December, President Mitterrand told the press that France was opposed to the militarization of space; he stressed that the major strategic objective should be disarmament and characterized the SDI program as "overarming" and potentially destabilizing. Two months later, at a conference on security policy in Munich, Defense Minister Hernu took up the same theme, expressing concern that the program would upset the strategic balance and launch a new arms race; Hernu went on to note in a March press interview that "American scientists are not sure it will work" and that, in any case, it "would not be completed before the end of this century. France and Europe must not demobilize." On the other hand, Foreign Minister Dumas, after his February trip to Washington, said that "differences have been narrowed."

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Comment. Hernu and other defense experts are concerned that SDI will prompt the Soviets to develop defenses that could defend against French missile attack and threaten the credibility of the French deterrent. If ballistic missile defense research does become a reality, Paris would prefer to lead an independent West European effort to develop such a defense. They will turn to cooperation with the United States only when they believe a joint European effort is not feasible. Thus, even if they have made up their own minds by early May -- which we deem unlikely -- the French will be reluctant to endorse a Summit declaration about SDI. They have a record of resisting general declarations on any subject that is not strictly relevant to the conference at hand. They are aware, moreover, that the Soviets will try to use West European concerns about SDI to divide the Alliance, and they prefer to avoid public discussions, especially at highly publicized forums like the Summit, that will present opportunities for differences to surface.

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UNITED KINGDOM

Prime Minister Thatcher supports research on SDI and welcomes the renewed arms control negotiations in Geneva; she probably will play down suggestions of Allied disunity. Foreign Secretary Howe said in a March interview that "the Soviets should not be allowed to drive a wedge between the Allies on SDI." Nevertheless, British politicians remain skeptical about SDI, and Howe, a close Thatcher ally, previously had expressed concerns over the cost and arms control implications of the program and emphasized the need to negotiate with Moscow before proceeding with deployment. Prime Minister Thatcher said in Parliament that Britain plans to adhere to the Camp David agreement on SDI worked out last December and reiterated that the 1972 Anti-Ballistic Missile Treaty signed by the US and the Soviets "permitted research but required negotiation before testing and deployment."

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Comment: Thatcher is interested in the technical aspects of SDI and may hope that London's unique ties to Washington would give the UK an advantage in sharing US technology. Like other Western leaders she faces increased nervousness at home over SDI, and probably will seek assurances at the Summit that Washington is willing to negotiate space defense systems with Moscow. She probably sees the Camp David formula as an appropriate Western position. Her strong personal support for SDI will be the key to overriding Foreign Office doubts and to paving the way for Defense Ministry cooperation with the US on SDI research. The Prime Minister remains sensitive to the prospect that an anti-missile system would undercut arguments for the Trident modernization program and probably would prefer to use SDI as a bargaining chip in Geneva rather than putting British forces on the line. Given Thatcher's stepped up diplomatic stance in East-West relations, more British interest in arms control issues is likely.

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ITALY

Prime Minister Craxi expressed his government's support for SDI development in his address to the US Congress this spring:

"We all wish that our security and world stability would no longer depend upon the reciprocal massive destruction capabilities of the two blocs. But today it is still necessary that our deterrent capacity be strong and that it be updated as the progress of science and technology continues relentlessly. We view with interest the research program for the Strategic Defense Initiative announced by President Reagan. Such a program appears to us as completely compatible with the existence of the ABM treaty, which must nevertheless continue to constitute an important reference point in the future negotiations in Geneva."

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In a March press interview, Foreign Minister Andreotti noted President Reagan's repeated declarations of the "clear separation" between SDI research and development. He went on to point out that although SDI had primarily military objectives, it also represented a potential for technological advancement that could not be ignored.

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Comment: We believe that Rome will continue to support SDI, but enthusiasm for the project will vary widely within the government. Defense Minister Spadolini is probably the most zealous advocate of SDI while Foreign Minister Andreotti is considerably more cautious. Most Italian officials probably view SDI as an unavoidable evil that the world simply will have to accept. Italian reservations about SDI are similar to those expressed by opponents in the US: they worry that moving toward defensive systems could destabilize East-West relations, decouple the US from Western Europe, upset chances for arms control in Geneva, and ultimately lead to greater expenditures on conventional weapons. On the other hand, Rome is intrigued by the technological aspects of the project and looks forward to exploiting its potential commercial applications.

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CANADA

Ottawa's wary attitude toward SDI is aptly reflected in two recent public statements by key officials:

"With regard to the question of any (Canadian) association with any aspect of the Strategic Defense Initiative, I can give the House of Commons assurance now, as I have before, that there is no plan, current, pending, or anticipated, that would have the Government of Canada involved in any way in the Strategic Defense Initiative." (External Affairs Minister Joe Clark, 5 February 1985.)

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"I suppose if somebody came forward and said, would we be interested in bidding for part of an SDI contract which would create, say, 10,000 jobs in Canada I think we would have to look at it." (Prime Minister Mulroney, 23 March 1985.)

Comment: SDI is receiving a tremendous amount of media coverage in Canada -- most of it skeptical or hostile -- and the Tory government is under daily pressure in the House of Commons from the political opposition. Press reports also suggest that the Cabinet is split on the issue of participation, with External Affairs Minister Clark leading opponents, Defense Minister Nielsen leading the advocates, and Prime Minister Mulroney somewhere in the middle. Nevertheless, the Tories have recently been indicating that SDI participation could increase employment in Canada and may thus be preparing to use economic arguments on behalf of accepting the US invitation. Mulroney almost certainly would prefer to reject participation, but he probably fears that he would alienate Washington and damage his campaign for better bilateral economic and political relations.

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[REDACTED] 25X1

EUROPEAN COMMUNITY

[REDACTED] EC Commission President Delors surprised reporters on the eve of the March EC summit by raising the possibility of Community participation in SDI. He noted that "if the Europeans are going to participate in a dispersed fashion, there will not be such a positive result as if they acted together." [REDACTED] 25X1

Comment: According to diplomatic reporting, Delors' comments about SDI mark the first time a Commission President has publicly addressed defense issues. Delors probably made the remarks to underscore the importance the Commission attaches to high technology research and development programs in the EC. [REDACTED] 25X1

25X1

25X1